Progressive EQUITY RESEARCH

ANEXO GROUP

BUSINESS SUPPORT SERVICES

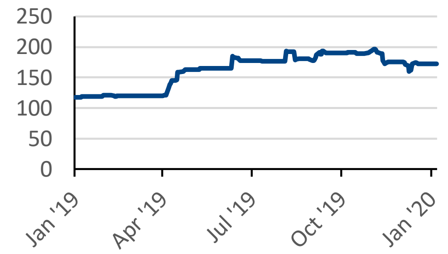
13 January 2020

ANX.L

172p

Market Cap: £189.8m

SHARE PRICE (p)



12m high/low	197p/118p

Source: LSE Data

KEY DATA

Net (Debt)/Cash	£(24.6)m
Enterprise value	£214.4m
Index/market	AIM
Next news	Prelims, March 2020
Shares in Issue (m)	110.0
Executive Chairman	Alan Sellers
CFO	Mark Bringloe
Bond Turner MD	Samantha Moss

COMPANY DESCRIPTION

Anexo is a specialist integrated credit hire and legal services group.

www.anexo-group.com

ANEXO GROUP IS A RESEARCH CLIENT OF PROGRESSIVE

ANALYSTS

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End-to-end action

Specialist integrated credit hire and legal services

Anexo Group has established itself as a provider of an end-to-end litigated claims service to predominantly impecunious non-fault motorists. It provides replacement vehicles – either from its own fleet or leased - and associated legal services. It has a highly experienced management team with experience in both credit hire and legal services. Thorough vetting of potential claims backs a high pre-court settlement rate. Its legal services business, Bond Turner, conducts the processing of the claim against at-fault motorists and their insurers and secures settlement. Currently targeting more measured growth in credit hire while recruiting more high-quality litigators, Anexo is increasing its capacity to settle cases and improve cash generation. By executing on its growth strategy and managing that balance between new business generation and cash collection from existing cases, we expect Anexo to produce strong earnings growth and cash generation.

- EDGE is the Group's specialist credit hire and initial claims management business which operates through two divisions offering a complete solution for non-fault motorists: DAMS – which provides cars and light commercial vehicles - and McAMS – which provides motorcycles.
- Bond Turner is the Group's legal practice which acts on all claims generated by EDGE. It seeks to recover hire charges and repair costs from at-fault insurers which can include damages for personal injury.
- Anexo wins customers through referral by a network of 1,150 local body shops and repairers. Its customers are typically impecunious and tend not have options to access a replacement vehicle which allows the Group to charge credit hire rather than spot hire rates, recovering these charges from the at-fault insurer at no upfront cost to the customer.
- With no fees paid on cases which include personal injury claims, the referring businesses benefit from the retention of the customer for any repair work and recovery fees for work approved by an independent engineer. Anexo may also pay a flat marketing retainer in return for the Group's advertising at the referrer's premises.
- There is plenty of scope for Anexo to grow in the UK with the number and success of its fee earners in collecting cash driving future opportunities for the Group. As it does that, we believe that its increased scale will make it more difficult for both new entrants and existing competitors to compete.

FYE DEC (£M)	2017	2018	2019E	2020E	2021E
Revenue	45.3	56.5	78.0	88.5	100.5
Adj EBITDA	15.8	18.7	26.9	30.9	35.0
Fully Adj PBT	14.6	16.1	23.2	26.1	28.5
Fully Adj EPS (p)	11.1	11.8	16.9	19.1	25.4
EV/Sales (x)	4.7x	3.8x	2.7x	2.4x	2.1x
EV/EBITDA (x)	13.5x	11.4x	8.0x	6.9x	6.1x
PER (x)	15.5x	14.7x	10.2x	9.0x	6.8x

Source: Company Information and Progressive Equity Research estimates

An integrated service for impecunious motorists

Originally a standalone credit hire business, the Group took on its current form with the incorporation of Armstrongs Solicitors, now renamed Bond Turner, in 2006. Since then, Anexo has provided a complete litigated claims process, which is predominantly focused on the recovery of credit hire and repair costs. The Group was admitted to AIM in June 2018.

EDGE is the Group's credit hire business which contains two key divisions offering a complete solution for non-fault motorists: DAMS – which provides cars and light commercial vehicles - and McAMS – which provides motorcycles. It also has a smaller unit which deals with bicycles. It operates a direct capture model for its referrals via 1,150 local body shops and repairers who are sourced and managed by a sales force of 20 people spread across the country. Edge also has a team of experienced claims handlers who are responsible for collecting information on road traffic accidents (RTAs) and assessing the validity of claims. The Group operates currently in England and Wales.

Bond Turner is the Group's legal practice which acts on all claims generated by EDGE. It seeks to recover hire charges and repair costs from at-fault insurers which can include damages for personal injury. Bond Turner also provides advocacy which is headed by Alan Sellers with the Group utilising external barristers as necessary to support the legal process.

The Group adopted an Alternative Business Structure licensed by the Solicitors' Regulation Authority (SRA) which allows non-lawyers to own and invest in law firms. Bond Turner is regulated by the SRA. DAMS is registered with the Financial Conduct Authority (FCA).

Within Bond Turner, Anexo also owns PALS which is a medical legal agency which arranges expert third-party reports to support the customer's claim from either a credit hire and/or personal injury perspective. The PALS team consists of 16 people and includes individuals experienced in claims processing and NHS procedures regarding medical records. Typically, all claims require engineer's and/or medical reports. Bond Turner instructs PALS on behalf of the client and any associated costs form part of the claim against the at-fault insurer.

IGCA administers after-the-event (ATE) insurance policies which are designed to cover the costs incurred in pursuing credit hire claims. These are offered to customers of EDGE at no extra cost. Policies are available for cases involving costs in pursuit of a personal injury claim and these are once again available to customers of EDGE, although these incur a charge which is payable at the end of the claims process. An ATE insurance policy covers claimants if they are found liable to pay their opponent's costs and solicitor's disbursements incurred as a result of them bringing a legal action.

At the interim stage of 2019, Anexo's vehicle fleet comprised 979 cars/vans and 1,938 motorcycles. Of those, 706 cars and 1,198 motorcycles were available for hire. Non-utilisation reflects vehicles deployed for internal use in fleet management (and therefore not available for hire) and those awaiting maintenance. Anexo hires its cars (mainly, they are Vauxhall and Mercedes) with its motorcycles predominantly owned and sourced from Yamaha – to the extent that Anexo is Yamaha's biggest customer in Europe. Anexo owns its motorcycles of 125cc and below, although there is an element of hire purchase involved. More powerful motorcycles are leased.

With further consolidation likely in the wider claims management market, Anexo will have the opportunity to grow market share as smaller law firms change strategy and exit the market. In terms of its geographic spread, the Group could also expand its regional coverage further to cover new areas of England and Wales. Following the success of the new Bolton office, the Board is also considering additional locations for a further regional office. In addition, the in-house advocacy and specialist litigation team within Bond Turner is also earmarked for expansion.

Definition of impecunious

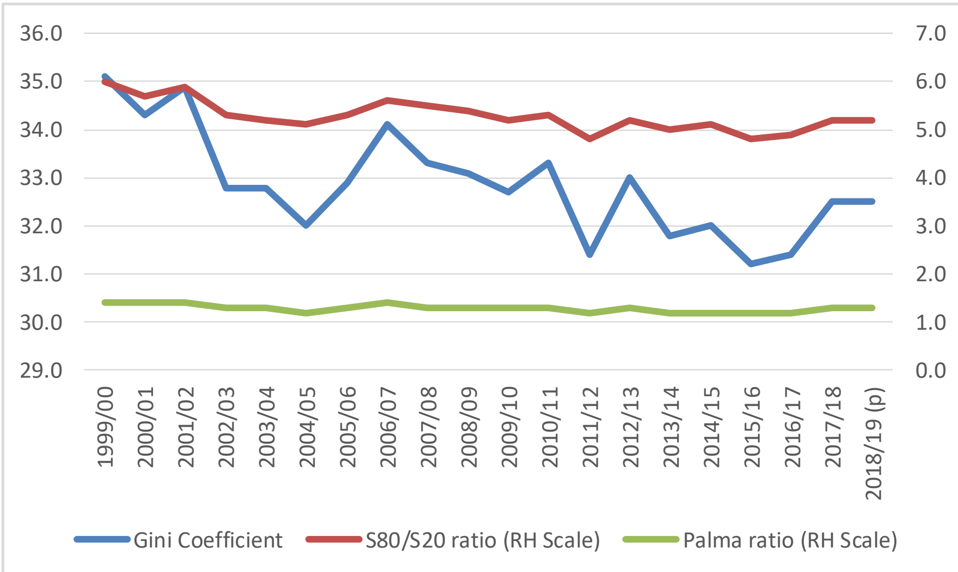
An impecunious claimant is generally deemed to be an individual who does not have immediate access to funds for a replacement vehicle. The term is not defined by statute but has been interpreted by the courts as referring to a claimant whose specific financial circumstances mean that he or she is unable to pay in advance for the hire term without making an 'unreasonable financial sacrifice', and therefore has no choice but to hire a replacement vehicle on credit terms.

Wealth distribution in the UK

Although it is difficult to estimate the size of the pool of impecunious people who are motorists and might become customers of Anexo, we would highlight the level of wealth disparity in the UK. There are several indices which are published by the Office for national Statistics (ONS) which show the spread of disposable income in the country.

- In economics, the Gini coefficient is a measure of statistical dispersion intended to represent the income or wealth distribution of a nation's residents. It is the most commonly used measurement of inequality. A value of 0 corresponds to the absence of inequality, so that, having adjusted for household size and composition, all individuals have the same household income. A value of 1 corresponds to inequality in its most extreme form, with a single individual having all the income in the economy.
- The S80/S20 ratio measures the relative disparity in the distribution of a given order of magnitude which means that, for an income distribution, it compares the mass of income held by 20% of the richest people to that held by 20% of the poorest people.
- Also a measure of inequality, the Palma ratio is the ratio of the richest 10% of the population's share of gross national income divided by the poorest 40%'s share.

Indicators of income inequality in the UK based on disposable income



Source: Office for National Statistics

The ONS release on household inequality, which gave provisional figures for the financial year ending 2019, showed that income inequality in the UK remained stable at 32.5%

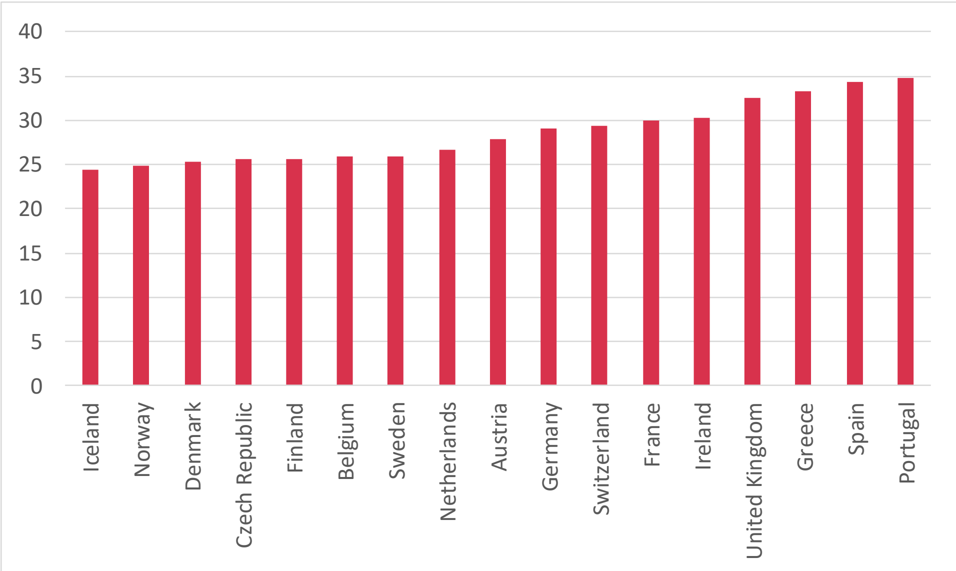
The S80/S20 ratio highlights that the richest fifth of people had a share of income that was over five times that for the poorest fifth in FYE 2019 – the same as it was in FYE 2018.

The Palma ratio highlights that the richest 10% of people accounted for a greater share of income than the poorest 40%, again, the same as the prior year.

The chart below shows where the UK sits in relation to a number of comparable European nations with regard to the Gini Index. Although the spread is over a limited range, the UK is towards the higher end of that range.

These economic measures won't indicate the level of impecuniosity in a country, but we think that they are a helpful indicator of income disparity and a reminder that a significant proportion of the population will fall into the category of needing financial assistance in the event of unexpected financial demands.

2018 Gini Index



Source: OECD

One might also look at the number of people who claim benefits from the Department of Work and Pensions. As at February 2019, 20 million people were claiming DWP benefits, of whom two-thirds were claiming the State Pension. Again, this is nothing more than a potential indicator of a pool of people who might require financial assistance. We would not consider, for instance, that all those claiming State Pensions would necessarily fall into that category.

The legal precedents that support Anexo's business model

Anexo Group operates in an environment which relies on legal precedent to support its business model. There have been suggestions that insurers will continue to pursue court cases to attempt to invalidate Anexo's ability to be party to the cases in which it becomes involved or to prove that its contracts are unenforceable. However, the history of credit hire litigation suggests that previous cases have tightened legal precedent in such a way that supports Anexo's business model.

Is there a risk of regulatory or legislative interference in the process? Given the legal precedents and the fact that Anexo's service is focused on impecunious customers, it would appear to be unlikely that regulators or legislators would wish to undermine the ability of those customers to gain access to replacement vehicles. However, in our view, it must remain a theoretical possibility that the level of damages may come under further scrutiny – although, again, legal precedent supports Anexo's position. Insurers could, of course, come to agreements with Anexo to settle cases at lower rates. In those circumstances, we would expect the quid pro quo to be a considerably faster time period for settlement which would allow Anexo to redeploy its cash back into new cases at a faster rate than it is currently able.

The chart on the following page seeks to summarise the relevant UK court decisions which have developed the legal backdrop to credit hire claims for impecunious clients. It shows the background, the relevant result or decision and the consequent impact on Anexo. Clearly, one of the most crucial cases is House of Lords ruling in Clark v Ardington (2003) that non-fault accident victims deemed impecunious have the right to recover credit hire rates from third party insurers. This ruling effectively underpins Anexo's business model and its ability to reclaim credit hire rates from at-fault insurers.

Credit hire litigation – UK court decisions and commentary

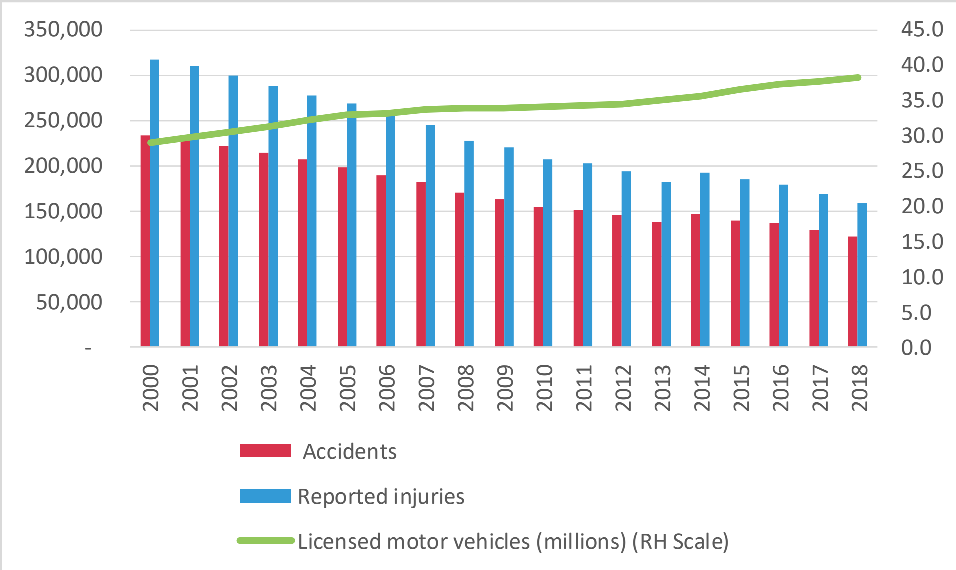
	1994	2002	2003	2004	2009	2011	2015	2015
	Giles v Thompson	Dimond v Lovell	Clark v Ardington	Lagdon v O'Connor	Copley v Lawn	Pattni v First Leicester	Stevens v Equity SM	Umerji v Khan
Background	Champerty (unlawful intervention in litigation by a third party), maintenance and need	Consumer protection compliance	Enforceability of credit hire agreements	Impecuniosity	Making amends	Burden of proof of reasonableness of credit hire rate	Burden of proof of reasonableness of credit hire rate	Hire period and claimants financial status
Result	House of Lords decided that agreements with credit hire companies were not unlawful	Credit hire agreements did not breach the Consumer Credit Act 1974	Court of appeal: Signed credit hire agreements were binding. Claim for hire charges quantifies damages for loss of use	Lord Hope: An impecunious motorist with no choice but to hire a replacement vehicle on a credit hire basis was entitled to the full cost	Suggested that insurers could take a reasonable step of supplying replacement vehicles to curtail claims for credit hire	Court of Appeal codified the principles governing the calculation of damages for credit hire.	Court of Appeal further identified that the rate for non-impecunious claimant must be from a mainstream supplier	Claimant is entitled to hire pending inspection of his vehicle whether they are impecunious or not
Result	There is a prerequisite to demonstrate that there was a need for a replacement vehicle	Consumer Credit Act subsequently amended making enforceability arguments rare	Court of appeal: ABI rates not to be used as a comparator for credit hire rates as those rates were not available to the public		Court of Appeal guided that any such offer should be appropriate with full information provided and independent advice available	Court of Appeal stated that the claimants were entitled to a like-for-like vehicle and that impecunious claimants are entitled to a full rate of hire	It further stated that the supplier must be in the claimant's locality and relevant to the model hired	Court allowed 140 days of hire
Impact on Anexo	Credit hire agreements are enforceable	Anexo had already altered its credit hire agreements to be compliant with consumer protection legislation before this case	Anexo can charge and seek to recover commercial credit hire rates	Anexo can charge and seek to recover commercial credit hire rates	Insurers rarely choose this option due to cost and admin considerations. Claimant could still recover a daily rate of hire equal to an insurer's offer	Underscores Anexo's rates to impecunious customers while burden of proof on rates charged to non-impecunious is on at-fault insurer	Underscores Anexo's rates to non-impecunious customers but not applicable to non-impecunious customers	Effectively rules out insurers' attempts to suggest short term limits on hire periods for non-impecunious claimants

Source: Company information and Progressive Research interpretation

Road Traffic Accidents (RTAs) and claims

At the end of June 2019, UK Government vehicle licensing statistics showed that there were 31,842k cars, 4,103k light goods vehicles and 1,332k motorcycles registered in Great Britain. The number of road traffic accidents (RTAs) reported in Great Britain in 2018 was over 122,000 according to Department of Transport statistics.

Vehicles and RTAs in Great Britain



Source: Department of Transport

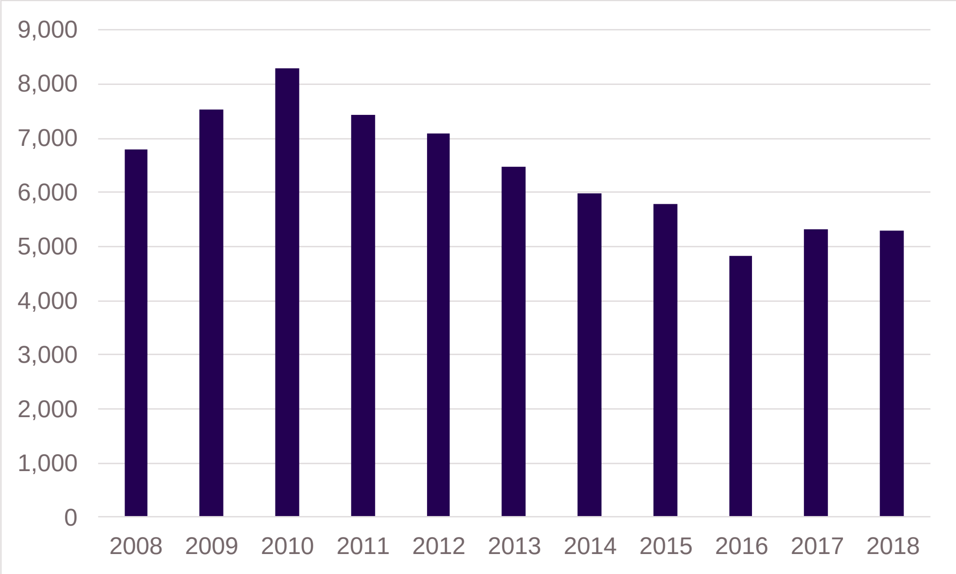
Although reported accidents and associated injuries have been on a declining trend, the number of events remains significant. Consequently, Anexo has a considerable market to address.

The Competition and Markets Authority (CMA) used a figure of 301,000 credit hire claims per annum when calculating the consumer detriment arising from the provision of replacement vehicles in its 2014 report, citing work previously carried out by the Ministry of Justice. We believe that this figure was associated with claims that included a personal injury claim. However, there are no clear industry-wide figures to verify that number or, more importantly, to update it.

Data from the Association of British Insurers shows the total motor claims for the last eleven years with recent years being around £5-6 billion per annum.

In December 2015, the Government replied to a petition on personal injury claims and noted in its response that “The number of reported road traffic accidents has fallen from approximately 190,000 in 2006 to around 146,000 in 2014 (a reduction of over 20%). However, at the same time, the number of road traffic personal injury claims has risen from around 520,000 in 2006/07 to 760,000 in 2014/15 (an increase of around 50%).” The background to its response included the Government’s intention “to crack down on false or unnecessary personal injury claims and the compensation culture”.

Net Motor Claims Incurred (£m)



Source: Association of British Insurers

In general, claims management companies (CMCs) gather cases either by advertising or through a direct approach. A claims manager may act for the client to pursue a claim or can operate as an intermediary between the claimant and the lawyers who may represent them. Claims managers have made money from several sources:

- referral fees from solicitors
- commission on auxiliary services
- after the event insurance and
- loans to the client

In April 2013 a ban on referral fees paid between CMCs, lawyers, insurers and others for personal injury claims was introduced which had a significant impact on the personal injury claims market. As a result, more than 1,000 CMCs left the sector, having been unable to adapt or change their business models to comply with the ban.

More specifically in the area which Anexo targets, CMCs can work with insurance companies or on their own, providing credit and legal services to non-fault motorists which may include the management of a claim to assist with the repair of a vehicle, provision of a replacement vehicle during the repair or replacement process and any associated legal claim.

The Jackson reforms

It is worth commenting a little more on the legal position on referral fees with reference to how Anexo maintains its relationship with its network of referring garages. In 2013, the Jackson Reforms on referral fees came into force which prohibited referral fees for personal injury claims. Consequently, Anexo does not pay fees to referrers in cases where a personal injury claim is involved. So, what benefits do referrers receive from their relationship with Anexo if they cannot be remunerated for referrals which include personal injury claims? The integrated service offers the retention of the customer for any repair work and recovery fees for work approved by an independent engineer. Crucially for small businesses that make the referrals, it can also provide accelerated payment of invoices for the work which it has been retained to carry out in relation to a claim being handled by Anexo. In certain instances, the Group also pays a flat marketing retainer (ie one which is static over a period of time and unrelated to the number of referrals) in return for the Group's advertising at the referrer's premises.

Competing CMCs?

Anexo's management does not think that there is a directly comparable competitor operating in the UK – mainly because of its integrated services offering, national positioning and focus on impecunious customers. Other credit hire and personal injury firms may compete to capture the customer immediately after an RTA. However, the former often operate under either GTA hire rates or with bi-lateral agreements with insurers resulting in a lower risk process free of litigation. Others may focus more on potential personal injury claims with the credit hire, repair and recovery elements tending to be less of a priority. For example, there are local firms of solicitors which may use a small number of vehicles as a tool to assist in seeking PI claims. Given the changes to legislation on personal injury claims contained in the Civil Liability Bill in April 2019 (currently scheduled to become effective April 2020), these companies are likely to come under further pressure during the coming year and many have already closed. Despite the lack of total comparability, we highlight some of the companies where we think there is some overlap with Anexo's businesses.

Comparator companies

Company	Current EV	EBITDA		EV/EBITDA		Share price	EPS		PER		LFY Yield
		CY1E	CY2E	CY1E	CY2E	(p)	CY1E	CY2E	CY1E	CY2E	(%)
Anexo Group PLC	**211.3**	**26.9**	**30.9**	**7.8**	**6.8**	**172.5**	**16.9**	**19.1**	**10.2**	**9.0**	**1.3**
DWF Group PLC	525.3	48.4	65.1	10.9	8.1	123.2	9.4	13.0	13.1	9.5	0.8
Gateley Holdings PLC	239.5	20.8	22.4	11.5	10.7	206.0	13.7	14.8	15.0	13.9	5.0
Keystone Law Group PLC	172.1	5.7	6.6	30.1	26.0	563.0	14.4	16.3	39.0	34.6	2.2
Law firms				**17.5**	**14.9**				**22.4**	**19.3**	**2.7**
Burford Capital Ltd	1677.0	338.9	398.2	4.9	4.2	678.0	126.6	146.1	5.4	4.6	0.6
Litigation Capital Management Ltd	54.7	6.5	9.6	8.5	5.7	69.8	4.5	9.5	15.5	7.4	n.a.
Manolete Partners PLC	159.3	4.3	6.4	37.5	24.9	431.0	17.2	22.7	25.1	19.0	0.3
Funders				**17.0**	**11.6**				**15.3**	**10.3**	**0.5**
Redde PLC	364.3	58.4	60.2	6.2	6.1	107.4	13.4	13.4	8.0	8.0	11.1
NAHL Group PLC	65.9	16.0	19.1	4.1	3.4	98.4	15.0	17.3	6.6	5.7	8.3
Hertz Global Holdings Inc	15272.0	510.0	591.1	29.9	25.8	1241.5	108.7	127.5	11.4	9.7	n.a.
Acident managers/hire companies				**13.4**	**11.8**				**8.7**	**7.8**	**9.7**

Source: Thomson Reuters, Progressive Equity Research

How does Anexo generate revenue?

EDGE hires out cars, vans and motorcycles to non-fault motorists. For the most part its customers are classed as impecunious and therefore they are able to claim credit hire rates rather than spot hire rates or GTA rates. Anexo's litigation business, Bond Turner then looks to recover the costs associated with a case – including any repair costs, storage expenses and personal injury damages.

The Group works on a no-win, no-fee basis so that there is no upfront cost to the customer (including hire and repair charges). Bond Turner seeks to recover costs from the at-fault insurer, typically through a litigated claims process on behalf of the customer.

This means that in the early stages of the process – until the end of the hire period - Anexo is incurring costs which are reflected in the Income Statement and through the Cash Flow Statement. It is also recognising a proportion of the associated revenues of a claim in the Income Statement and on the Balance Sheet. However, at this point, there are clearly no revenue cash flows. Bond Turner then takes the claim through the recovery process with debts collected on successful claims on average 500+ days into the process with an average settlement rate of around 56%.

The outlook for cash is clearly related to cases worked and settled. However, Anexo follows strict protocols on revenue recognition through the income statement and it is useful to understand at what stage the two main parts of the business report their revenues and how the cash flow follows that accounting process.

How does Anexo recognise revenue?

Prepayments and accrued income

Prepayments and accrued income of £24.9 million at the interim stage included around £10 million of work-in-progress (WIP) relating to vehicles on the road based on average settlement rates. The Credit Hire business recognises a proportion of the amount chargeable when a vehicle hire is completed. It books 47% of revenues during the life of a claim (effectively taking an initial 53% provision on a portfolio basis) with any uplift resulting when cash settlement is made perhaps some 15-18 months later. Bond Turner essentially reflects cash accounting and takes a flat fee on admission of liability.

Credit Hire

- Revenue from the supply of credit hire vehicles is recognised over time from the date a vehicle is placed on hire, excluding VAT. It is accrued on a daily basis, adjusted for recoverability based on historical settlement rates.
- Upon conclusion of an individual hire, the claim is invoiced and accrued income associated with that hire written back to nil.
- Revenue recognised is updated on settlement once the amount of fees that will be recovered is collected.
- If not collected within four years, accrued income is written back to nil.

Legal Services

- Revenue from the rendering of legal services to customers is recognised upon delivery of the service to the customer.

- Fees are earned only in the event of a successful outcome of a customer's claim. These are generally a fixed fee plus a percentage of damages recovered.
- Accrued income represents client cases which have not yet reached a conclusion and is carried at a value that includes profit of prescribed fixed fees at the earliest stage post issue of proceedings.
- Initial revenue recognised in WIP reflects the minimum fee (around £1,160 which is the minimum fee generated on a personal injury claim) to which the Group is entitled once an admission of liability has been confirmed.
- Value is only attributed to cases which are less than three years old.
- Revenue recognised is updated (and removed from accrued income) on settlement once the actual amount of fees that will be recovered is collected.

Trade Receivables

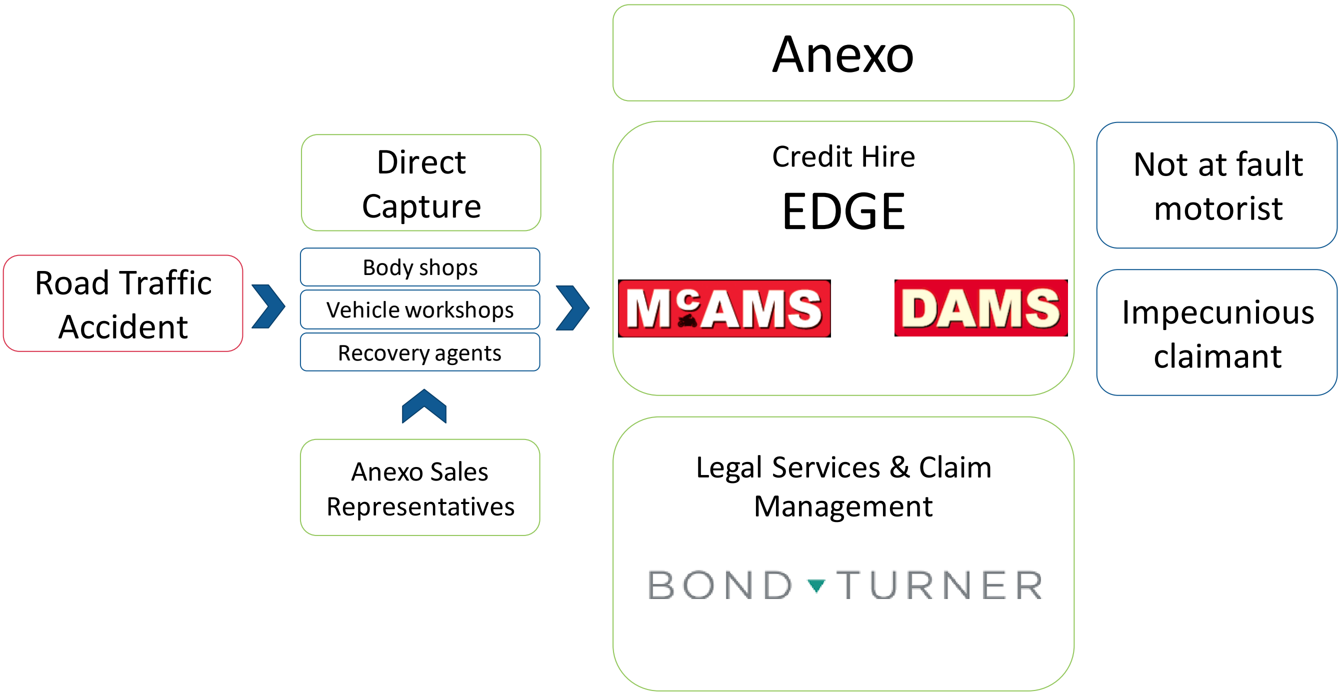
Trade receivables are initially measured at fair value less transaction costs and subsequently carried at amortised cost less any allowance for discounts and impairment. For example, at the interim stage of FY 2019, Anexo reported Net Trade Receivables of £89.9 million. Of that amount, around £63 million was for credit hire fees after provisions for recoverability. Another £7 million represented repair fees due from at-fault insurers. Repair, recovery and storage costs are paid from working capital by Anexo on behalf of their clients. These amounts are generally fully recovered and consequently do not appear in the Income Statement. The credit hire fees will have already been recognised.

The backlog of cases within Bond Turner stood at 20,392 at the interim stage of 2019. Of that total, around 12,000 cases included credit hire with the remainder reflecting passenger and other claims. Given the Group's accounting policies there is a sizeable block of potential unrecognised revenue not reflected in the Balance Sheet. As we note elsewhere, the associated cash flow follows at the end of the case when settlement is received. We note that management has been clear in its intention to tackle the backlog while maintaining the fleet size during FY 2020E and this is reflected in our outlook for the growth opportunities open to the Group.

Winning business

Following an RTA, individuals are put in touch with EDGE by recommendation through its direct capture model. The claim is then allocated to DAMS or McAMS according to the vehicle type.

Capturing customers

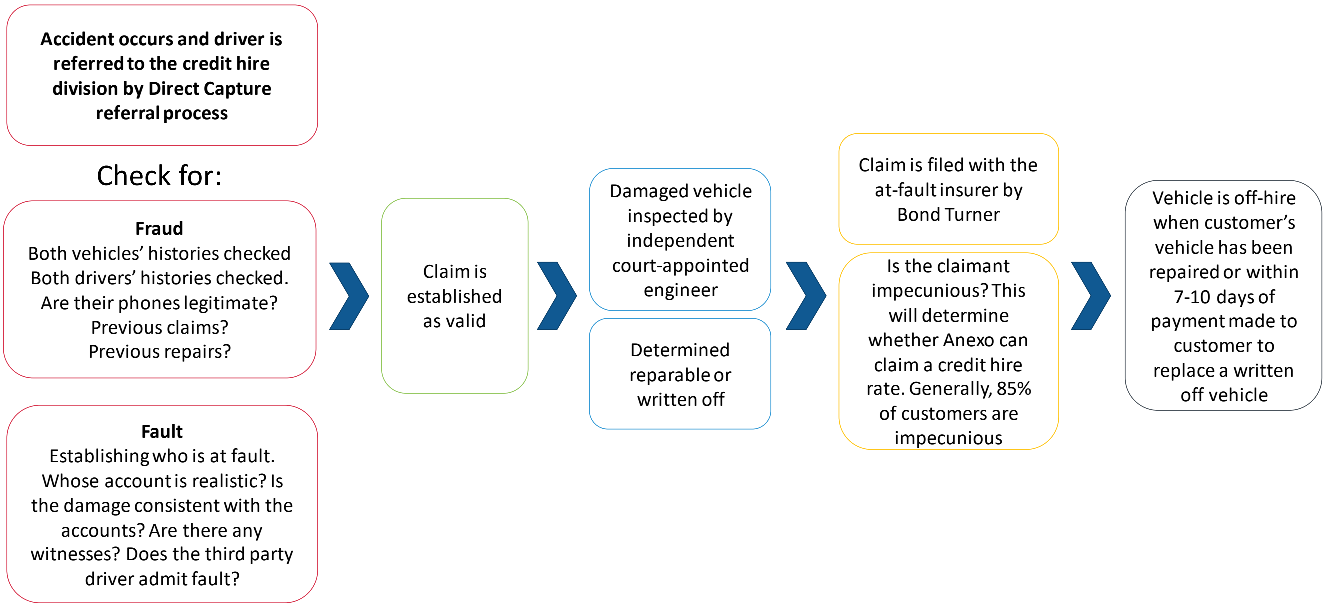


Source: Company information, Progressive Equity Research

EDGE has 22 claims handlers of whom eight are bi-lingual. They make the initial investigations to establish liability and take customers statements and collate information, including witness statements. Customers complete a questionnaire over the telephone and the claims handlers will assess the validity of the claim in conjunction with the other information available and the completion of maps and road analysis. An assessment team with over 20 years of claims experience also conducts a risk assessment of each claim. It will, for instance, check whether drivers or witnesses have been involved in a previous claim in any capacity. The resulting success rate of vetted claims is over 98%. In 2018, the Group accepted around half of the 12,000 opportunities which were presented to the Group.

When accepted, the claim follows the process in the following chart.

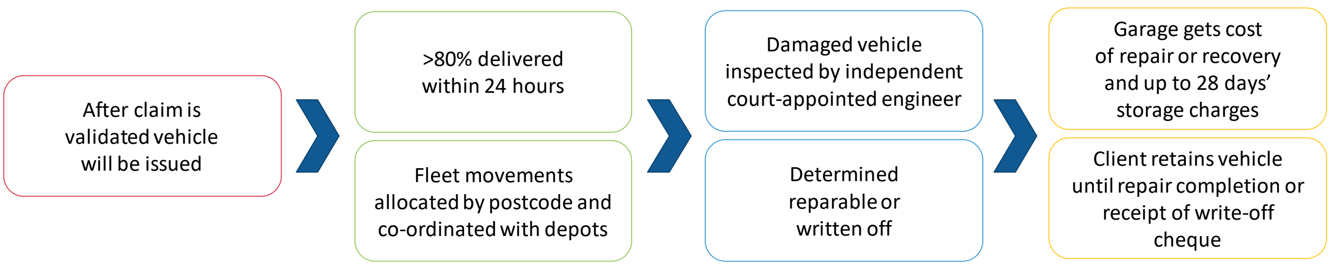
Vetting a potential claim



Source: Company information, Progressive Equity Research

The delivery of a replacement vehicle to the customers follows from the initial validation of the claim. That means that it is not known whether the customers is impecunious at the time of the vehicle being delivered.

Issue of vehicle



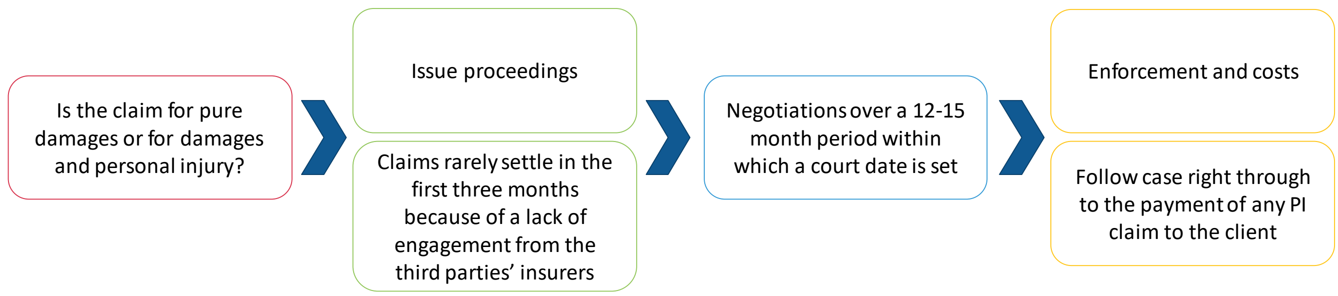
Source: Company information, Progressive Equity Research

On average, the fleet of vehicles has a utilisation rate of c.85%. Cars have a utilisation rate of 72%, vans (generally sourced from third party suppliers) 93% and motorcycles 89%. Following their return after a hire term, cars are valeted and checked for roadworthiness within 24 hours and motorcycles are checked and serviced within 48 hours to allow them to be available for the next customer.

Bond Turner's involvement reflects its service to the customer throughout the process following the acceptance of the validity of the claim. It ensures compliance with court orders and collects cash once settlement has been agreed.

Initially, claims are established as pure damages or damages plus personal injury cases. Bond Turner will issue proceedings against at-fault insurers and will conduct negotiations, following the case through to conclusion when the customer receives payment. The business includes its own in-house barristers in its advocacy/court department.

The claim process for credit hire claims



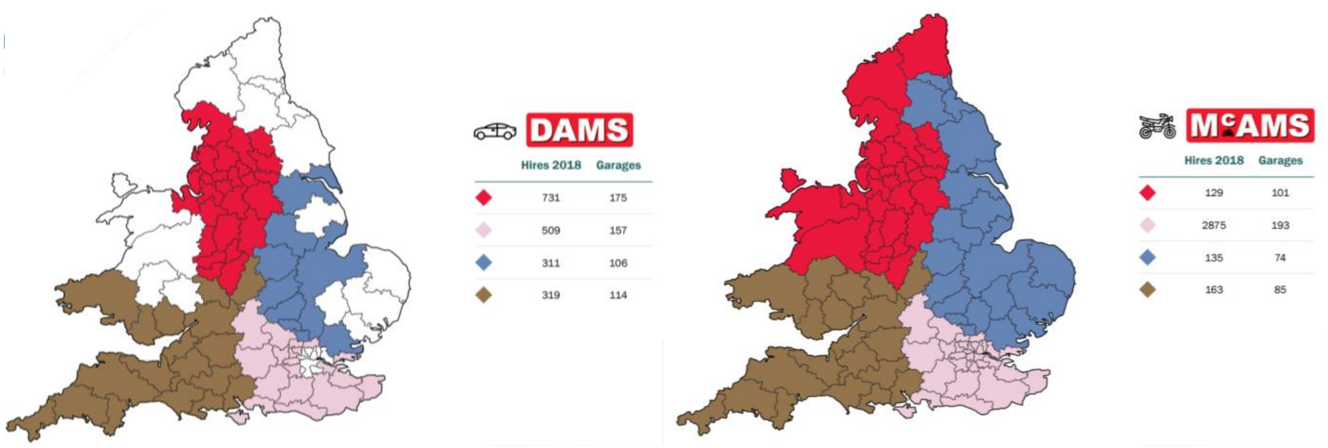
Source: Company information, Progressive Equity Research

Growth opportunities

With further consolidation likely in the wider CMC market, Anexo will have the opportunity to grow market share in a consolidating market as law firms change strategy and exit the market. We have heard from management at the recent Capital Markets Day that the Group will have a particular focus on cash collection during the coming year – particularly in light of the significant backlog of cases which it has on its books at present. We therefore expect that Bond Turner will continue to increase the number of solicitors and legal assistants that it employs to process and settle the cases. In turn, this will release cash back into the Group and enable Edge to take on more cases. Once a more optimal balance has been achieved between the generation of new cases and the settlement rate, we would expect Edge to increase the number of vehicles available for hire and employ additional sales representatives. There is also an argument for enlarging the number of barristers directly employed by Anexo as the workload increases in house so that work does not need to be given to other chambers.

In terms of its geographic spread, the Group could also expand its regional coverage further to cover new areas of England and Wales. The chart below, produced by Anexo, shows the geographic coverage of England and Wales by Edge's sales staff and its network of referrers for DAMS and McAMS. The respective hires made during 2018 and the number of garages for each is also shown. There is clearly scope to expand the coverage of DAMS and to deepen the penetration which McAMS has in its existing coverage.

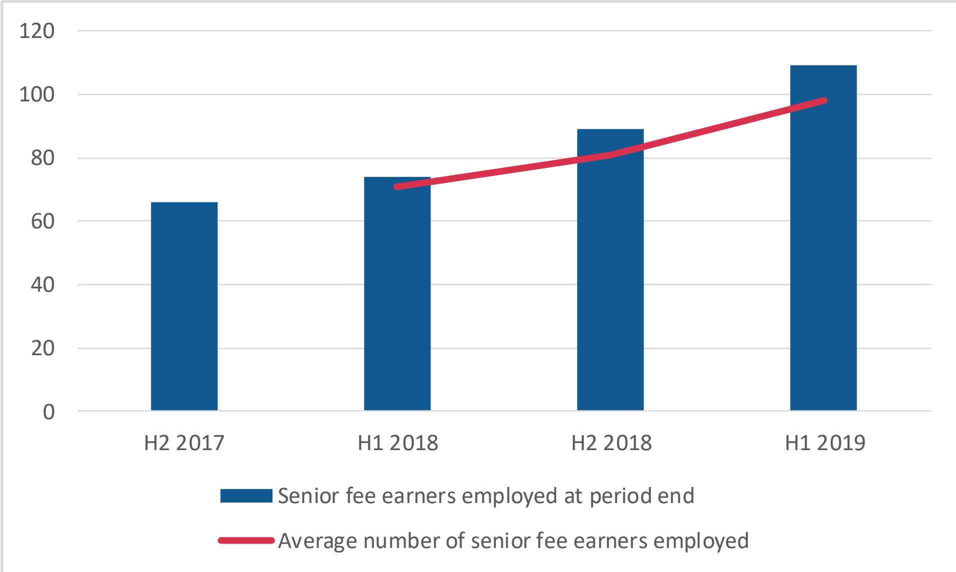
Edge – Coverage in England and Wales



Source: Company information

The example of Bond Turner's new Bolton office is a useful example of how its capacity can be raised. The office opened in December 2018 and by the end of June 2019 it employed 28 senior litigators an was in the process of recruiting more. In fact, at that stage, recruitment had continued to progress faster than anticipated. The Group had consequently finalised the terms of a lease for a further floor in Bolton, doubling the office space.

Bond Turner headcount



Source: Company information

The Board is also considering additional locations for a further regional office and will make a separate announcement as and when appropriate. The additional capacity secured to date has already positively impacted cash collections and settlement numbers and rates.

The in-house advocacy and specialist litigation team within Bond Turner is also earmarked for expansion. The team handles complex professional and clinical negligence claims and the cases can be high value and high profile. In its interim results announcement, the Group provided the example of the class action concerning historic abuse at Aston Hall psychiatric hospital. There is a specific intention to expand the specialist team further in FY 2020 and the Board is 'exploring opportunities to secure new business in professional and compensation claims through both targeted recruitment and digital marketing and direct capture'.

Example case

The chart on the following page shows a timeline of the involvement of the two Anexo businesses in a theoretical 'average' car hire claim. The whole process can take up to 500+ days until settlement is achieved and outstanding debts are collected – although some cases clearly may settle earlier or later than that average outcome. The chart also shows when revenues are booked and costs are incurred. To give a broad example of the relative scale of the relevant figures, the table below shows our estimates based on our interpretation of the numbers reported by Anexo or commented on by management at previous analysts' meetings. The differences between the booking of revenues and the relevant cash flow is a point we shall return to later. Bond Turner settled 2,066 cases in the first half of 2019, up from 1,974 in the corresponding period in 2018. It has a 98% success rate in winning pre-court settlements. Most cases take well over a year to settle – only 2-3% settle within the first three months.

Management has previously noted that Bond Turner tends to get maximum traction on case settlement between 12 and 24 months of a case timetable. Insurers tend to be the main barrier to quick settlement and therefore much of this delay is out of Anexo's hands. Anexo engages via the insurers' claims portal in a process which allows the insurers to view evidence for a 90 day period. If they do not respond following that period, Anexo will issue court proceedings with the insurers eventually seeking settlement when a court date is imminent. As we highlight earlier, insurers could, of course, come to agreements with Anexo to settle cases at lower rates – and the Group does have some protocol agreements with a few insurers. Meanwhile, in general, the longer timescale applies to the majority of Anexo's cases.

One of the key things to note is the final amount recovered of £9,163 as a proportion of the credit hire cost of £15,600 in our example. At 58.7%, it is a little higher than the rate most recently reported by Anexo of 56.5%, reflecting the various assumptions which we have made. There are several reasons why settlements are around this level:

- Few cases are clear-cut with a 100% fault allocation. Hence, there may be varying elements of contributory negligence to take into account which will results in the recovery of inly a proportion of fees.
- When a case is first taken on, financial information about the customer is not always immediately available. If a customer turns out not to be impecunious then only the spot hire rate may be recoverable (typically around 50% of the credit hire rate).
- Bond Turner may take a view on any offer received and the ultimate likely recoverability and choose to accept a settlement rate which is optimal for a particular case and which frees up funds to be reinvested in new cases.

We would expect to see the Group aim to improve its settlement rate, perhaps to around 60% over time, but this would be dependent on the cases it takes on.

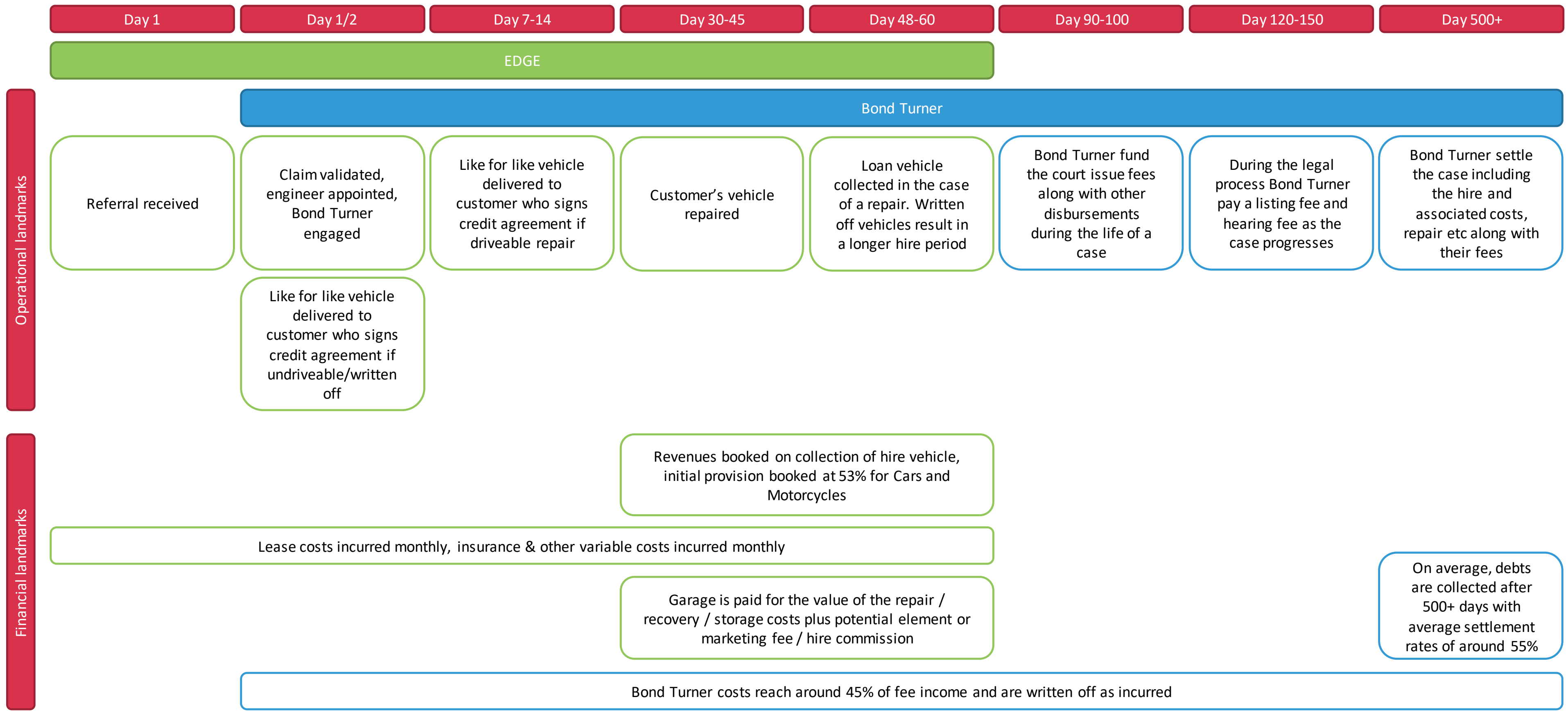
Example revenue and disbursements for a car hire claim case

		Assumptions
	Hire period (days)	65
	Average daily hire	£240
	Total hire cost	£15,600
	Repair cost	£3,500
	Personal injury	£2,000
	Total claim	**£21,100**

Case days		Income Statement	Balance Sheet	Cash Flow
0 - 60	Lease costs	(£700)		(£700)
0 - 60	Insurance & other variable costs	(£1,100)		(£1,100)
48 - 60	Revenues booked on collection of the vehicle	£15,600	£15,600	
	Initial provision booked at 53%	(£8,268)	(£8,268)	
30 - 60	Garage is paid for the value of the repair / recovery / storage costs	(£650)	£3,500	(£4,150)
	Position at the end of hire	**£4,882**	**£10,832**	**(£5,950)**
90 - 120	Bond Turner funds the court issue fees and other associated costs during the life of a case		£1,055	(£1,055)
120 - 150	Bond Turner pays a listing and hearing fee		£600	(£600)
550	Bond Turner settles the case	£5,515		£5,515
550	Debt collected	£1,248	(£12,487)	£13,735
	Bond Turner staffing costs	(£2,482)		(£2,482)
	Position after settlement and collection	**£9,163**	**£ -**	**£9,163**

Source: Progressive Equity Research estimates

Credit hire case – Operational and financial landmarks

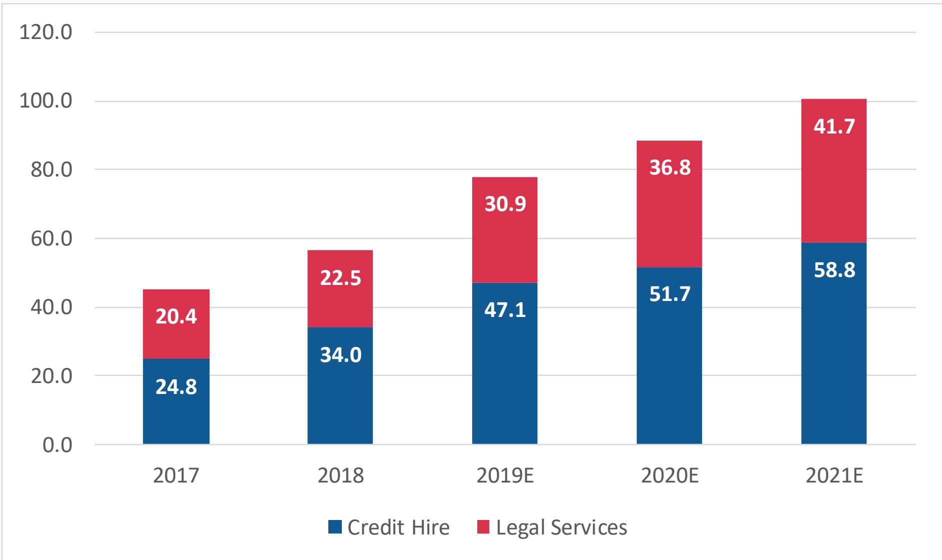


Source: Company information and Progressive Research interpretation

Estimates

We note that Anexo has said that its focus for the coming financial year is on cash collections. This is particularly driven by the number of fee earners/litigators that it employs and the number of cases which they are able to manage and settle in any one year. Prior to its IPO, the Group was constrained on how much new business it could write by its lack of capital. Given the removal of that constraint with the capital raised during the IPO process, the Group has now developed a surplus of cases which it needs to reduce by hiring more litigators to increase the rate at which the outstanding cases are settled. That will naturally free up cash to be reinvested in new cases but we expect that to be deliberately reined in during FY 2020E so as not to overwhelm the litigators further. Thereafter, we expect to see a balanced growth of both sides of the business to allow cash collections to fund new business and to produce a reduction in net debt over time.

Revenue (£m)



Source: Company information, Progressive Research estimates

Income Statement (£m)

	2017	2018	2019E	2020E	2021E
Revenues	45.3	56.5	78.0	88.5	100.5
Cost of sales	(11.3)	(16.2)	(19.9)	(22.2)	(25.2)
Gross Profit	**34.0**	**40.3**	**58.1**	**66.3**	**75.2**
Gross Profit (%)	74.9%	71.4%	74.5%	74.9%	74.9%
Central costs	(18.1)	(21.6)	(31.2)	(35.4)	(40.2)
Total S, G & A	(18.1)	(21.6)	(31.2)	(35.4)	(40.2)
Research & Development	0.0	0.0	0.0	0.0	0.0
Other expenses / income	0.0	0.0	0.0	0.0	0.0
Profit post central costs	**15.8**	**18.7**	**26.9**	**30.9**	**35.0**
Depreciation	(0.8)	(1.6)	(2.1)	(3.0)	(4.1)
EBITDAA pre dep pre all amortisation	**15.8**	**18.7**	**26.9**	**30.9**	**35.0**
EBITDA Margin	*35.0%*	*33.2%*	*34.5%*	*34.9%*	*34.9%*
Restructuring costs (exceptional)	0.0	(1.4)	0.0	0.0	0.0
Share based payments	0.0	(0.4)	(0.4)	(0.4)	(0.4)
Total Interest	(0.5)	(1.1)	(1.7)	(1.8)	(2.5)
Profit before tax	**14.6**	**14.3**	**22.8**	**25.7**	**28.1**
Tax	(2.1)	(2.9)	(4.1)	(4.6)	(5.1)
Tax rate (%)	*14.4%*	*20.2%*	*18.0%*	*18.0%*	*18.0%*
Profit after tax	**12.5**	**11.4**	**18.7**	**21.1**	**23.0**
Dividends	0.0	0.0	(2.8)	(2.8)	(3.2)
To reserves	**12.5**	**11.4**	**15.9**	**18.3**	**19.8**
Adjusted PBT	14.6	16.1	23.2	26.1	28.5
Adjusted PAT	12.5	13.2	19.0	21.4	28.5
Adjusted attributable earnings	12.5	13.2	19.0	21.4	28.5
Per share data					
No of shares (million)					
Undiluted, period-end	110.0	110.0	110.0	110.0	110.0
Undiluted, average	110.0	110.0	110.0	110.0	110.0
Fully diluted, average	112.2	112.2	112.2	112.2	112.2
Diluted EPS (p)	11.1	10.2	16.6	18.8	20.5
Adj. Diluted EPS before exc. items (p)	11.1	11.8	16.9	19.1	25.4
Dividend (p)	0.0	1.5	2.2	2.7	3.2

Source: Company information, Progressive Research estimates

Balance Sheet (£m)

	2017	2018	2019E	2020E	2021E
Gross tangible assets	3.6	6.3	10.1	14.1	18.6
Acc. depreciation	(2.0)	(3.1)	(5.1)	(8.1)	(12.2)
Net Tangible Fixed Assets	1.5	3.3	5.0	6.0	6.4
Total Fixed Assets	**1.5**	**3.3**	**5.0**	**6.0**	**6.4**
Current Assets					
Accrued income	16.2	22.5	28.2	31.2	34.9
Trade debtors	55.9	76.0	95.3	105.6	118.0
Deferred tax	0.0	0.1	0.1	0.1	0.1
Other debtors	8.5	2.9	2.9	2.9	2.9
Cash & equivalents	0.2	5.5	1.2	6.9	12.4
Total current assets	**80.8**	**107.0**	**127.6**	**146.8**	**168.2**
TOTAL ASSETS	**82.3**	**110.2**	**132.6**	**152.7**	**174.6**
Creditors < 1 year					
Loans and Overdrafts	(9.8)	(21.9)	(24.9)	(24.9)	(24.9)
Trade Creditors	(5.4)	(7.2)	(9.7)	(11.5)	(13.6)
Other	(6.0)	(4.4)	(4.4)	(4.4)	(4.4)
Total	**(21.2)**	**(33.6)**	**(39.1)**	**(40.9)**	**(42.9)**
Net Current Assets	**59.6**	**73.4**	**88.5**	**105.9**	**125.3**
Total assets less current liabilities	61.1	76.7	93.5	111.9	131.7
Creditors > 1 year					
Borrowings	(5.5)	(0.9)	(0.9)	(0.9)	(0.9)
Other	0.0	0.0	(1.0)	(1.0)	(1.0)
Total	**(5.5)**	**(0.9)**	**(1.9)**	**(1.9)**	**(1.9)**
NET ASSETS	**55.6**	**75.8**	**91.7**	**110.0**	**129.8**
Capital and Reserves					
Called up share capital	0.1	0.1	0.1	0.1	0.1
Share Premium	0.0	9.2	9.2	9.2	9.2
Unappropriated profit	0.0	0.4	0.4	0.4	0.4
Profit and Loss Account	55.5	66.1	82.0	100.4	120.2
Currency translation & other	0.0	0.0	0.0	0.0	0.0
Shareholders funds	55.6	75.8	91.7	110.1	129.9
CAPITAL & RESERVES	**55.6**	**75.8**	**91.7**	**110.1**	**129.9**

Source: Company information, Progressive Research estimates

DAMS uses an invoice discounting facility which is secured on the trade receivables of that company, the balance outstanding being reported within bank loans and overdrafts.

Cash Flow (£m)

	2017	2018	2019E	2020E	2021E
EBIT before associates	**15.1**	**15.4**	**24.5**	**27.5**	**30.6**
Add back : depreciation	0.7	1.6	2.1	3.0	4.1
Stock (increase)	0.0	0.0	(5.7)	(3.1)	(3.6)
Debtors (increase)	(12.4)	(20.9)	(19.3)	(10.4)	(12.3)
Creditors (decrease)	(0.3)	1.8	2.5	1.8	2.1
Operating Cash Flow	**3.1**	**(2.1)**	**4.1**	**18.8**	**20.7**
Net interest	(0.5)	(1.1)	(1.7)	(1.8)	(2.5)
Dividends paid	(3.7)	(0.8)	(2.8)	(2.8)	(3.2)
Taxation	(1.5)	(4.7)	(4.1)	(4.6)	(5.1)
CAPEX	(1.5)	(4.7)	(3.8)	(4.0)	(4.5)
Trading Cash Flow	**(4.0)**	**(13.5)**	**(7.3)**	**5.7**	**5.5**
Short term investments	0.0	1.8	0.0	0.0	0.0
Sales of fixed Assets	0.2	0.2	0.0	0.0	0.0
Shares issued	0.0	9.2	0.0	0.0	0.0
Net debt change	**(3.8)**	**(2.2)**	**(7.3)**	**5.7**	**5.5**
Net (debt) / cash	**(15.0)**	**(17.3)**	**(24.6)**	**(18.9)**	**(13.4)**

Source: Company information, Progressive Research estimates

Dividend policy

The Board has adopted a progressive dividend policy since Admission, paying 1.5p for the period from Admission to 31 December 2018. The Board expects to follow a progressive dividend policy, although the amount will be subject to determination at the applicable time. Anexo declared an interim dividend of 1.0p per share for the first half of 2019.

Employee share plan

Anexo operates a Management Incentive Plan (MIP) through its Executive Growth Share Plan. The Group granted MIP awards on 20 June 2018 to key employees, via its subsidiary, Edge Vehicles Rentals Group Limited (EVRGL). They were granted C ordinary shares in EVRGL which can be converted to Anexo Group Plc shares or converted to cash if the Group achieves set profit after tax targets:

- £9.9 million for 31 December 2018
- £11.9 million for 31 December 2019 and
- £13.9 million for 31 December 2020.

Assuming the profit targets are met 50% of the awards will vest on 31 December 2021 and the remaining 50% vest on 31 December 2022. Management intend to settle the scheme in Anexo Group Plc shares. As at 31 December 2018 there were 2.2 million MIP awards outstanding. The target was met for 2018 and our estimates for the following two years are significantly above the remaining hurdles.

The Board

Alan Sellers, Executive Chairman

Alan Sellers was called to the Bar in 1991 at the Gray's Inn Bar and is currently practising from the Liverpool Civil Law Chambers. Alan is an expert in civil litigation, personal injury and credit hire claims and clinical and professional negligence, and he is recognised as a leading figure in these fields. Mr Sellers was one of the founders of the business and has been instrumental in forming Anexo Group plc as it operates today. On admission, Mr Sellers will continue to practise as one of Anexo's in-house team of barristers.

Mark Bringloe, Chief Financial Officer

Mark Bringloe is a Chartered Accountant having previously worked at Ernst & Young, Robson Rhodes and BDO. Mark was Director in BDO's Corporate Finance team prior to working as a consultant. Mark joined Anexo in 2009 before subsequently joining the Board as Chief Financial Officer.

Samantha Moss, Bond Turner Managing Director

Samantha Moss graduated from the University of Manchester with a degree in law and accountancy in 2003 and she was subsequently admitted as a solicitor in 2008. Samantha has worked at Bond Turner since 2004 and is currently Managing Director. Samantha is a specialist in clinical and professional negligence and civil litigation, including personal injury and credit hire claims. Samantha also maintains managerial responsibility for Bond Turner and overseas regulatory compliance, client care, complex claim, staff supervision, account and complaints handling. Samantha is married to Alan Sellers.

Christopher Houghton, Senior Independent Non-Executive Director

Christopher Houghton is a fellow of the Chartered Institute of Management Accountants. He joined Park Group plc in 1986 in a finance role rising to Finance Director in 2001. After taking on operational responsibilities he became Chief Executive in 2012 retiring from the group in 2018.

Richard Pratt, Independent Non-Executive Director

Richard Pratt was called to the Bar in 1980 and has practised in Liverpool, specialising in criminal law. He was appointed a QC in 2006 and has been the head of his chambers since 2012 and leader of the Northern Circuit between 2011 and 2013. Richard is also a recorder of the Crown Court.

Roger Barlow, Independent Non-Executive Director

Roger Barlow is a Chartered Accountant and was a partner with KPMG until 2000. Since then he has held a number of directorships and is currently Senior Independent Non-Executive Director and Chair of Audit at a challenger bank, Bank & Clients plc. He is the independent member of the Audit Committee at the Information Commissioner's Office and was recently Chairman of Marsden Building Society and also Chair of Audit at a NHS Foundation Trust Hospital. He has also been CFO and Chairman of two AIM listed companies.

Elizabeth Sands, Independent Non-Executive Director

Elizabeth Sands is currently Chairman of Great Bowery, a New York based fashion agency back by Private Equity. She has also provided independent advice to a number of both private and public companies including a FTSE100 utilities company and an international investment bank. She was previously Head of Organisation and Transformation UK at AT Kearney following which she was Vice Chair of the Finance and Investment, and Workforce committees at the Devon Partnership NHS Trust.

Risks

Risk	Risk/impact	Management action/comments
Changes to legislation (case law or statutory changes)	Any reduction in fee income will directly affect profit levels.	Education of key staff members, monitoring of changes in case law and statute.
Government actions and legal developments	Credit hire revenues rely on the House of Lords ruling that non-fault accident victims deemed impecunious have the right to recover credit hire rates from third party insurers.	The Group keeps abreast of developments.
New costs within the business necessary to maintain business levels	A rise in payment of issue fees and hearing fees to litigate cases would directly affect cash requirements	Closely monitor costs and review monthly. Management can make a commercial decision to increase settlement and conclude cases.
Retention of key fee earners and senior management	Loss of key lawyers or inability to attract new lawyers could significantly impair the strategy, operations and financial condition of the Group	Maintenance of staff satisfaction levels and an ongoing recruitment policy. Staff trained from a junior level and supported to ensure retention. Key lawyers are incentivised.
Losing cases	The Group invests heavily in cases that are reliant on a successful outcome for recovery of money. Money is only received upon successful conclusion of any claim.	Review of circumstances around those cases that are lost. Assess risk/benefits of new business. Consideration of merits of appealing cases. Ensure that potential claims are properly vetted. Train and employ staff to increase chance of successful outcome and use specialised counsel. Employ fraud team.
Network and systems performance	Disruption to operations impeding work and risking damage to reputation and customer relationships.	Ongoing, regular extensive reviews and testing.
GDPR/personal data	If breaches of personal data occur, damages can be claimed and large fines are payable. This has financial and potential reputational implications.	Regular staff training on GDPR legislation. Regular review and risk assessment of processes. Ongoing reviews of systems relating to any complaints.
Retention of garages and sources of work	Garages that advertise DAMS services could be enticed by other deals from competitors.	Nurture garages through education, offer competitive deals, and train them into understanding compliance with LASPO, Code of Conduct and FCA rules.
Increased competition	The Group could face competition from other companies that offer similar products and services in the broader credit hire and PI sector.	Any direct competitor would have to be a new entrant to the market or a change in existing business model, incurring very high set up costs. Anexo monitors the market and continues to offer competitive product. Invests in development of the service.
Litigation	The Group is a highly litigious firm. Adverse costs arising from litigation will negatively impact the Group's financial as well as cause potential reputational damage from losing cases.	Extensively and continuously discussed with management and fee earners to ensure awareness. Although it seeks to minimise adverse costs, some cannot be avoided in entirety due to clients' inability to reply fully and in a timely fashion, draconian court orders and the hostile nature of litigation.
Regulation	Compliance with Code of Conduct, Solicitors Accounts Rules, any applicable FCA rules, GDPR, Statute (LASPO) etc.	Ensure regulatory compliance is monitored through updated policies, staff training, spot checks and audits. Conduct risk assessments to identify any areas of weakness or potential breach. Monitor and record any complaints/feedback.
Bank covenants	Monitored on a daily basis. Staff awareness training is regularly provided. Constant review and reporting to the bank on covenants	Monitored on a daily basis. Staff awareness training is regularly provided. Constant review and reporting to the bank on covenants

Source: Company information, Progressive Equity Research

Financial Summary: Anexo Group

Year end: December (£m unless shown)

PROFIT & LOSS	**2017**	**2018**	**2019E**	**2020E**	**2021E**
Revenue	45.3	56.5	78.0	88.5	100.5
Adj EBITDA	15.8	18.7	26.9	30.9	35.0
Adj EBIT	15.1	17.2	24.9	27.9	31.0
Reported PBT	14.6	14.3	22.8	25.7	28.1
Fully Adj PBT	14.6	16.1	23.2	26.1	28.5
NOPAT	15.1	17.2	20.4	22.9	31.0
Reported EPS (p)	11.1	10.2	16.6	18.8	20.5
Fully Adj EPS (p)	11.1	11.8	16.9	19.1	25.4
Dividend per share (p)	0.0	1.5	2.2	2.7	3.2
CASH FLOW & BALANCE SHEET	**2017**	**2018**	**2019E**	**2020E**	**2021E**
Operating cash flow	3.1	(2.1)	4.1	18.8	20.7
Free Cash flow	(4.0)	(13.5)	(7.3)	5.7	5.5
FCF per share (p)	(3.7)	(12.3)	(6.6)	5.2	5.0
Acquisitions	0.0	0.0	0.0	0.0	0.0
Disposals	0.0	0.0	0.0	0.0	0.0
Shares issued	0.0	9.2	0.0	0.0	0.0
Net cash flow	(3.8)	(2.2)	(7.3)	5.7	5.5
Overdrafts / borrowings	(15.2)	(22.8)	(25.8)	(25.8)	(25.8)
Cash & equivalents	0.2	5.5	1.2	6.9	12.4
Net (Debt)/Cash	(15.0)	(17.3)	(24.6)	(18.9)	(13.4)
NAV AND RETURNS	**2017**	**2018**	**2019E**	**2020E**	**2021E**
Net asset value	55.6	75.8	91.7	110.0	129.8
NAV/share (p)	50.6	68.9	83.3	100.0	118.0
Net Tangible Asset Value	1.5	3.3	5.0	6.0	6.4
NTAV/share (p)	1.4	3.0	4.6	5.4	5.8
Average equity	27.8	65.7	83.8	100.9	120.0
Post-tax ROE (%)	57.8%	35.2%	31.2%	28.2%	0.0%
METRICS	**2017**	**2018**	**2019E**	**2020E**	**2021E**
Revenue growth		24.7%	38.0%	13.5%	13.5%
Adj EBITDA growth		18.4%	43.7%	14.8%	13.4%
Adj EBIT growth		14.0%	44.8%	12.1%	11.0%
Adj PBT growth		10.3%	44.0%	12.8%	9.0%
Adj EPS growth		5.7%	43.9%	12.8%	32.9%
Dividend growth		N/A	46.7%	22.7%	18.5%
Adj EBIT margins		30.4%	31.9%	31.5%	30.8%
VALUATION	**2017**	**2018**	**2019E**	**2020E**	**2021E**
EV/Sales (x)	4.7	3.8	2.7	2.4	2.1
EV/EBITDA (x)	13.5	11.4	8.0	6.9	6.1
EV/NOPAT (x)	14.2	12.5	10.5	9.4	6.9
PER (x)	15.5	14.7	10.2	9.0	6.8
Dividend yield	N/A	0.9%	1.3%	1.6%	1.9%
FCF yield	(2.1%)	(7.1%)	(3.8%)	3.0%	2.9%

Source: Company information and Progressive Equity Research estimates

13 January 2020

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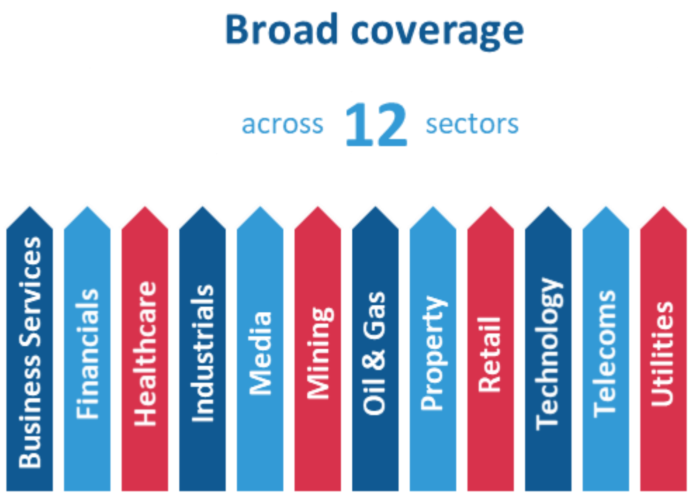

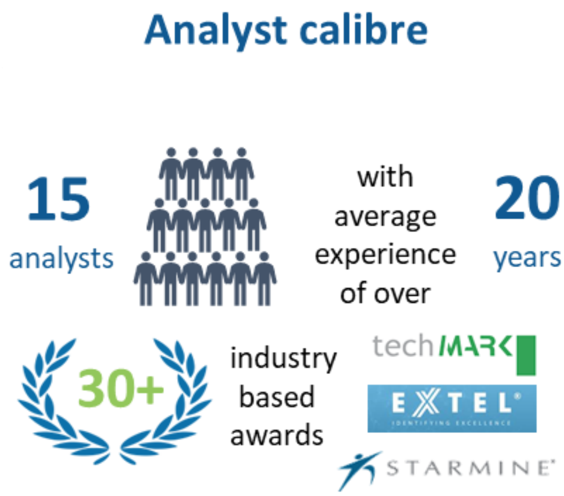

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